



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Number: **201332015**
Release Date: 8/9/2013

Date: May 14, 2013

UIL: 501.08-00

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear :

This is our final determination that you do not qualify for exemption from federal income tax as an organization described in Internal Revenue Code section 501(c)(8). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

You must file federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, you should follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your federal income tax status and responsibilities, please contact IRS Customer Service at

Letter 4040 (CG) (11-2005)
Catalog Number 47635Z

1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933.
The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Holly O. Paz
Director, Exempt Organizations
Rulings and Agreements

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



**DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224**

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: March 26, 2013

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

LEGEND:

X= organization

B = state

C = date

D = individual

e = dollar amount

f = dollar amount

UIL: 501.08-00

Dear :

We have considered your application for recognition of exemption from federal income tax under Internal Revenue Code section 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under Code section 501(c)(8). The basis for our conclusion is set forth below.

Issue

Do you qualify for exemption under section 501(c)(8) of the Code? No, for the reasons stated below.

Facts

You were incorporated under the mutual benefit law of the state of B on C. You were previously granted exemption from federal income tax under section 501(c)(10) as a domestic fraternal society not providing life, sick, accident or other benefits to members. Your exemption was then revoked. You reapplied for recognition of exemption under section 501(c)(8) as a domestic fraternal society providing life, sick, accident or other benefits to members.

Letter 4034(CG) (11-2011)
Catalog Number 47628K

Section 2, Article II of your Amended Articles of Incorporation state your purposes are to:

Be operated under the lodge system. The net earnings of the corporation shall be devoted exclusively to fraternal, charitable and educational purposes. The Corporation shall provide for the distribution of a one-time cash payment of e dollars upon the death of any members. This is not a life insurance policy, but is simply a benefit of membership. Said payment shall be made to the beneficiary designated by the member in the most recent beneficiary designation form completed by the member and returned to the corporation during that member's period of membership in the Corporation. If, during the member's period of membership in the corporation, the member fails to complete and return a beneficiary designation form, no payment shall be made by the Corporation.

Your Bylaws authorize the creation of lodges in states where membership can reach at least five members. These lodges must agree to abide by your bylaws, be a member in good standing with you, and pay a per capita tax each December.

You indicate % of your time is devoted to providing funds to various child abuse agencies nationwide. However, you later indicated fundraising to support breast cancer, Amber alerts, and troopers in need. You accomplish this through a contract with X. You will also provide financial assistance to your members of f dollars per year for medical care and to the member's family in the event of the member's death by payment of e dollars. You offer a scholarship for e dollars to a child or grandchild of a member as well as a semi-annual informational newsletter to all members and other interested individuals and groups.

Your members must be retired from active police duty, eligible to retire from active duty, on disability or a surviving spouse of a former member. Member dues are g dollars, however, fund solicitation materials indicate you provide free membership and healthy benefits programs.

You have a comprehensive contract with X for professional fundraising services. Essentially all your income is from fundraising campaigns X conducts on your behalf. X has raised between dollars and dollars on your behalf. About % of this was for fundraising expenses paid to X. Approximately one percent of your total income was expended on charitable activities consisting of donations to various charitable organizations. The remaining % was used for your expenses including benefits to members, payroll and professional expenses.

Per your agreement, X conducts telephone and direct mail, public relations and fundraising campaigns on your behalf. Some of the provisions in the contract are:

- X will use its call center for you located in the state of B
- X will distribute brochures, tax receipts, or any other printed materials, provide entertainment, and other promotional materials on your behalf.
- You will either create written or solicitation materials or X may create these for you and you must approve all materials X uses.
- X will establish mailboxes for receiving mail for you. You acknowledge these mailboxes will not be exclusively dedicated to you and the mailboxes are X's property.
- X will receive your mail during the term of the agreement and during any wind down period of any fund raising campaign. You also acknowledge mail addressed to you may continue to be forwarded to X after the wind down period of any fund raising campaign .
- You must establish a bank account within 10 miles of X's account receivables department so X can deposit the funds raised on your behalf. Moreover, you must agree to maintain on record with each applicable bank an irrevocable written direction to the bank authorizing electronic transfer of the percentage of the gross deposits authorized in the contract to X the same day funds are deposited or the day the funds become available.
- You will not close any bank accounts without giving X ten days notice prior to closing said account. You agree not to close any such account during the term of agreement unless you have opened another bank account that meets the above requirements.
- You agree to enter into merchant accounts with certain credit cards so X can receive credit card donations for you.
- X has the right to conduct the campaign on your behalf and the fundraising is limited to the states described in the agreement; in addition, X's rights in the particular states shall be exclusive and you will not authorize any other person to solicit donors and/or funds on your behalf within the particular state.
- You will promptly review and complete any forms, registrations, certificates or other documents required by the governing body of any charitable organizations, federal, state or local governments, or professional solicitors within five days of receipt and return such forms, registrations and certifications, to the appropriate governing body and/or X within such time period.
- You will promptly review and return to X any forms, registrations, certifications, or other documents that X requires to fundraise within the particular state.
- You agree to conduct some of your programs in each of the states the funds are raised.
- The contract is long term in nature and calls for an automatic renewal of terms unless notification by one party 90 days in advance of the intent to terminate.
- The contract guarantees income to X based on prior year amounts.

You provided addendums to the contract to address compensation. Each addendum

was tailored to each particular state in which X was conducting fundraising and the percentage of compensation is based on the minimum amount of gross receipts required by state law. The amount of gross receipts you are entitled to is generally between % and % depending on state law. However, concerning the allocation of expenses the contract states:

The parties acknowledge and agree that in accordance with generally accepted accounting principles, expenses incurred as joint activities may be allocated among various expense categories. Therefore, X agrees to make available to an accountant who represents you such information that may be necessary to accomplish such allocations on your behalf.

You use D as your accountant who is contracted to represent you for all tax forms and matters including the Form 1024 application for recognition from federal income tax, Form 990 information return, Form 1120 income tax return, Form 941 employment tax, and Form W-2 income tax. In addition, D prepares financial reporting for X. You stated using the same CPA as X is not a conflict since you are not opposing groups and you stood nothing to lose by sharing a CPA.

Finally, you provided the following inconsistent information:

- You stated you are providing education campaigns to prevent child abuse but the most recent contract between you and X states you are providing educational programs on breast cancer awareness.
- Before your exemption was revoked, you had operations in several states but then you said you only have operations in 2 states. Your website still says you are operating in more than two states and X is still fundraising on your behalf in these states. You then stated you intend on operating in ten states. You provided no evidence that you have active lodges.
- You stated that you and individual lodges will be responsible for fundraising activities; however, you have contracted with X to fundraise in certain states and agreed to have programs in these states.
- On Form 1024 you indicate you intend on both operating (page 3) and not operating (part 2) under a lodge system

Around % of your funding over the past five years has come from 'direct public support', with around % of your income from member fees. Fundraising comprises around % of your expenses, with benefits, payroll and funeral expenses the next three largest. Around % of your annual expenses are contributions.

Law

IRC 501(c)(8) describes fraternal beneficiary societies, orders, or associations operating under the lodge system (or for the exclusive benefit of the members of a fraternity itself

operating under the lodge system), and providing for the payment of life, sick, accident, or other benefits to the members of such society, order, or association, or their dependents.

Section 501(c)(8) of the Code provides for the exemption from federal income tax of fraternal beneficiary societies, orders, or associations—

- (A) Operating under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under the lodge system, and
- (B) Providing for the payment of life, sick, accident or other benefits to the members of such society, order, or association or their dependents.

Section 1.501(c)(8)-(a) of the Regulations states that a fraternal beneficiary society is exempt from tax only if operated under the "lodge system" or for the exclusive benefit of the members so operating. "Operating under the lodge system" means carrying on its activities under a form of organization that comprises local branches, chartered by a parent organization and largely self-governing, called lodges, chapters, or the like. In order to be exempt it is also necessary that the society have an established system for the payment to its members or their dependents of life, sick, accident, or other benefits.

Rev. Proc. 2012-9, superseding Rev. Proc. 90-27, 1990-1 C.B. 514, Section 4.01, provides the Internal Revenue Service will recognize the tax-exempt status of an organization only if its application and supporting documents establish that it meets the particular requirements of the section under which exemption from federal income tax is claimed. Section 4.02 states that a determination letter or ruling on exempt status is issued based solely upon the facts and representations contained in the administrative record. It further states:

- (1) The applicant is responsible for the accuracy of any factual representations contained in the application.
- (2) Any oral representation of additional facts or modification of facts as represented or alleged in the application must be reduced to writing over the signature of an officer or director of the taxpayer under penalties of perjury statement.
- (3) The failure to disclose a material fact or misrepresentation of a material fact on the application may adversely affect the reliance that would otherwise be obtained through issuance by the Service of a favorable determination letter or ruling.

Section 4.03 states that the organization must fully describe all of the activities in which it expects to engage, including the standards, criteria, procedures or other means

adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures.

Rev. Rul. 78-87, 1978-1 C.B. 160, describes a situation in which possible benefit to non-exempt entities was determined to be incidental to the accomplishment of a 501(c)(8)'s purposes. The 501(c)(8) participated in a state sponsored reinsurance pool along with non-exempt insurers. There was concern that the non-exempt insurers would derive a benefit from the participation of the 501(c)(8) and its payments into the pool; however, any such benefit derived was determined to be incidental to the accomplishment of the 501(c)(8)'s exempt purposes.

The court in National Union v. Marlow 74 F. 775, 778-779 (8th Cir. 1896) stated that even if the member of an organization enjoys a common tie or goal, the organization does not serve a fraternal purpose unless its members engage in fraternal activities.

The court in Western Funeral Benefit Ass'n v. Hellmich, 2 F.2d 367 (E.D. Mo. 1924), stated that "by the 'lodge system' is generally understood as an organization which holds regular meetings at a designated place, adopts a representative form of government, and performs its work according to ritual."

In Philadelphia and Reading Relief Association v. Commissioner, 4 B.T.A. 713 (1926), the court held that an organization of railroad company employees that made payments to members who became disabled because of accident or sickness was not entitled to exemption because it was not "fraternal". The court cited rituals, ceremonies, and regalia as evidence of a fraternal purpose, and was unable to discover a single fraternal feature in its organization, being entirely without social features or fraternal object. The petitioner has neither lodges, rituals, ceremonial, or regalia; and it owes no allegiance to any other authority or jurisdiction.

In Fraternal Order of Civitans of Am. V. Comm'r, 19 T.C. 240 (1952) it was held that the mere recitation of common ties and objectives in an organization is governing instrument is insufficient to be classified as fraternal. There must be specific activities in implementation of the appropriate purposes.

Application of Law

You do not meet the provisions of IRC 501(c)(8) or section 1.501(c)(8)-(a) of the Regulations. You are providing death and health benefits to members, however, you do not have any activities that accomplish a fraternal purpose. In addition, you set up lodges in certain states so X could fund raise on your behalf in that state. You did not provide any information that these lodges are active or are conducting any fraternal activities. Your activity in these states is merely the donation of funds to charitable organizations. Like you, these lodges have been set up to enable X to operate.

You are not like the organization Rev. Rul. 78-87 because you are benefiting X in a substantial manner. Without the use of your tax exemption, X would not be permitted exclusive rights to fundraise on your behalf in certain states. X receives about 90% of the proceeds from the fundraising campaign. You do not have control and supervision of how funds are being raised. Most of the funds raised end up as compensation to X. The benefit X derives from the contract is not incidental and therefore this precludes exemption. Finally, D is the accountant for both you and X. Transactions between you and X are not arms-length.

You do not meet the definition of fraternal as provided in the National Union v. Marlow. You have not provided any evidence that you have rituals, ceremonies or regalia as described in the court case, Philadelphia and Reading Relief Association v. Commissioner. You indicate % of your activities are providing financial support to various non-profit organizations. The remainder is spent on member health/death/scholarship benefits, as well as a semi-annual newsletter. You have demonstrated no fraternal activities.

You do not operate under a lodge system as defined according to Western Funeral. You did not substantiate the existence of any lodges, only the plans on how lodges may be formed and fees they would pay. You did not describe any meetings or established locations or rituals.

You are similar to the organization in Fraternal Order of Civitans of Am. V. Comm'r, 19 T.C. 240 (1952). Even though your governing instrument indicates you have common ties and objectives, this is insufficient to be classified as fraternal. You do not have specific activities to accomplish fraternal purposes.

As required by Rev. Proc. 2012-9, you have not established that you are organized and operated exclusively for purposes described in Section 501(c)(8). You provided inconsistent and very general information concerning your lodges and your activities. The information you have provided indicates that you have no fraternal activities. As required by Section 4.03 of this Rev. Proc., you must fully describe all of the activities in which you expect to engage, including the standards, criteria, procedures or other means adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures. You have failed to provide adequate details to allow us to determine that you are operating primarily for fraternal purposes within the meaning of Section 501(c)(8).

Applicant's Position

Concerning the relationship with X, you simply could not reach the vast numbers of people that a professional company can and X raises money from new donors as well as donors that have contributed in the past through a detailed callback program. X approached you and offered to fund raise on your behalf and you selected them based

on their terms and reputation. You are also in the discussion stages of additional fundraising plans. You are reviewing your community partnerships to see how you might better capture donations at the local level. Concerning the conflict of interest D has, he is a licensed professional in the accounting field and provides professional services according to professional standards.

Service Response to Applicant's Position

You failed to provide any additional information from which it can be concluded that you qualify under Section 501(c)(8). You have not shown you are actively engaged in fraternal activities. Your contract with X indicates X is deriving a substantial benefit and has substantial control over your fundraising activities. Because D works for you and X your agreements are not arms-length.

Conclusion

You do not qualify for exemption under Section 501(c)(8) of the Code because you have not shown that you are substantially engaging in fraternal activities. In addition, your activities benefit X in a substantial manner. You have also not met the requirements to provide consistent and detailed information establishing you are qualified for exemption.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter.

We will consider your statement and decide if that information affects our determination. If your statement does not provide a basis to reconsider our determination, we will forward your case to our Appeals Office. You can find more information about the role of the Appeals Office in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*.

Types of information that should be included in your appeal can be found on page 2 of Publication 892, under the heading "Regional Office Appeal". The statement of facts (item 4) must be declared true under penalties of perjury. This may be done by adding to the appeal the following signed declaration:

"Under penalties of perjury, I declare that I have examined the statement of facts presented in this appeal and in any accompanying schedules and statements and, to the best of my knowledge and belief, they are true, correct, and complete."

Your appeal will be considered incomplete without this statement.

If an organization's representative submits the appeal, a substitute declaration must be included stating that the representative prepared the appeal and accompanying

documents; and whether the representative knows personally that the statements of facts contained in the appeal and accompanying documents are true and correct.

An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you during the appeal process. To be represented during the appeal process, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice Before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter to you. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to the applicable address:

Mail to:

Internal Revenue Service
EO Determinations Quality Assurance

Deliver to:

Internal Revenue Service
EO Determinations Quality Assurance

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Holly O. Paz
Director, Exempt Organizations
Rulings and Agreements

Enclosure: Publication 892